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No. 85-1035

In the Supreme Court of the United States

OCTOBER TERM, 1985

CROCKER NATIONAL BANK,

Appellant,

v.

PAUL PERDUE,

Appellee.

ON APPEAL FROM THE SUPREME COURT OF CALIFORNIA

BRIEF OF *AMICUS CURIAE* FIRST INTERSTATE BANK OF OREGON, N.A., IN SUPPORT OF APPELLANT CROCKER NATIONAL BANK'S JURISDICTIONAL STATEMENT

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INTERESTS OF AMICUS CURIAE

Appellant Crocker National Bank filed a jurisdictional statement with this Court, seeking review of a California Supreme Court decision. That decision rejected federal preemption and set the stage for state court regulation of national bank charges for checking account services. The particular charge at issue is the "NSF charge" that is levied when a customer over-

draws the checking account. Because of the importance of the questions involved in the appeal, First Interstate Bank of Oregon, N.A. ("First Interstate"), through its counsel, requested and received consent from both parties to the proceedings below to submit this brief in support of Crocker National Bank's jurisdictional statement.

Amicus First Interstate is a national bank. It provides, among many other services, checking accounts to customers throughout the State of Oregon. As a national bank, First Interstate is, of course, subject to federal banking laws and regulations.

In 1980, three plaintiffs filed suit in the Circuit Court for Multnomah County, Oregon, on behalf of a class of individual checking account customers estimated to number over 200,000. (*Tolbert, et al.* v. *First National Bank of Oregon* [now known as First Interstate], No. A8004-02328.)[1] This suit challenged First Interstate's $6 NSF charge on a variety of state common-law and statutory theories. The state trial court certified a class and rejected First Interstate's federal preemption argument. The case proceeded to trial in March 1985. Plaintiffs' theory at trial was that the

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[1] Four other cases challenging bank NSF charges were filed in Oregon state courts at about the same time as *Tolbert*. One was decided in the bank's favor on summary judgment and is now before the Oregon Court of Appeals; one issue there involves federal preemption. The three additional cases remain dormant, pending the outcome of *Tolbert* and the other Oregon case now on appeal.

NSF charge represented an invalid liquidated damage provision, or "penalty", instead of a service charge, such that the NSF charge must approximate the bank's processing cost. Plaintiffs asked for $12 million in damages, plus fees and costs, under this claim. After pretrial and trial proceedings totaling over a month, the jury returned a verdict in favor of First Interstate. Plaintiffs have appealed, and the appeal is pending before the Oregon Court of Appeals. Federal preemption is one of the issues on appeal.

A decision from this Court would resolve a key question now before the Oregon appellate courts. Indeed, a decision in favor of Crocker National Bank would terminate the controversy in *Tolbert*, to which this *amicus* is a party, and in the several other related Oregon cases. First Interstate, then, has a direct interest in having this Court correct the erroneous proposition that a state court may modify the price at which a national bank offers demand deposit accounts to the public.

SUMMARY OF ARGUMENT

This Court should exercise jurisdiction over this appeal because fundamental, undecided Supremacy Clause issues are at stake. In the absence of such exercise, the California decision will be used to effect improper and inconsistent state regulation of national banks. The entire pricing structure of national bank services in the newly competitive, deregulated market is affected.

Not only is the California decision far-reaching, it also is wrong. Conflict preemption exists because there is an extensive body of federal statutes and regulations opposed to the exercise of state authority sought by the plaintiff below and allowed by the decision at issue. In addition, field preemption exists because federal law already has occupied the field the state court is trying to invade: there is federal law on the issues of how NSF charges are to be set and what is a proper amount.

ARGUMENT

In one of its earliest cases, this Court saw the need to maintain the autonomy and stability of national banks. Chief Justice Marshall, writing for a unanimous court in *McCulloch* v. *State of Maryland*, 17 U.S. (4 Wheat.) 316 (1819), recognized the concept of preemption and confirmed that a state law may not "retard, impede, burden, or . . . control" federal enactments relating to the operations of national banks. 17 U.S. at 436.

A strong, stable national banking system is just as critical now as it was 160 years ago. The recent bank failures, the aggressive position of the FDIC, and the dependence of our entire economy on a sound national bank system all are factors that demonstrate the vital importance of the federal banking laws in our country today.

A state may, of course, regulate national banks. A state may not, however, interfere with a national

bank or supersede Congress's plans; such action is preempted under the Supremacy Clause.[2]

There are three methods by which federal preemption of state authority may occur.[3] The three methods are express preemption, implied preemption, and preemption by virtue of conflict between state and federal regulation. The second and third apply here. A state exercise of authority that conflicts with the network of federal banking laws and regulations, or impinges on an area of national bank law reserved by Congress, is unconstitutional under the Supremacy Clause.

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[2] "This Constitution, and the Laws of the United States which shall be made in Pursuance thereof . . . shall be the supreme Law of the Land . . . any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." U.S. Const. Art. VI, cl. 2.

[3] *Ray* v. *Atlantic Richfield Co.*, 435 U.S. 151 (1978); *Fidelity Federal Sav. & Loan Ass'n.* v. *De La Cuesta*, 458 U.S. 141 (1982); *Silkwood* v. *Kerr-McGee Corp.*, 464 U.S. 238, 104 S. Ct. 615, 621 (1984).

I

THE ISSUES IN THIS CASE ARE OF THE UTMOST NATIONAL SIGNIFICANCE.

A. The Decision Below Severely Alters the Character of the Banking Industry.

Federal banking laws, regulations, and policies provide for market pricing of national bank services. The California Supreme Court's ruling, if followed in other jurisdictions, will preclude national banks from using this uniformly market-driven system of pricing NSF services, and the ruling may be extended to preclude market pricing of all bank services. Thus, this case has the potential to work a radical transformation of one of the most basic concepts of national banking.

Suppose that, instead of a common-law theory, this Court were considering a state statute that established local boards to regulate bank pricing. Suppose further that these boards would act like public utility commissions; they would make rules to define "costs", require banks to submit economic evidence, and appoint industry experts to set tariffs. Those tariffs would, in our example, cover prices related to checking account services. There is no question that the Supremacy Clause would preclude application of this state regulatory system to national banks.

The decision below has done essentially the same thing. While the jury in the First Interstate case found as a factual matter that the NSF charge was a service charge, so that the market properly set the

price, the California Supreme Court has held the opposite. Under its holding, the market mechanism is forbidden to fix the NSF charge. Instead, in every instance a national bank must submit to a quasi-rate hearing before a lay jury, who will decide after the fact, and without standard guidance as to allowable accounting methods, whether the national bank's price was properly related to its costs. This result will be nothing short of revolutionary nationwide.

B. The California Supreme Court's View Heavily Burdens National Banks.

The impact upon this *amicus* of the issue presented here illustrates its enormous practical — as well as theoretical — importance to the national banking system. The First Interstate NSF case shows that the *burden*, in cost and time, of the assertion of a state-law claim is immense. Discovery spanned a period of over four years; the jury trial lasted over three weeks. Plaintiffs now are challenging First Interstate's victory in the Oregon appellate courts. This process will consume substantial additional resources unless this Court steps in to remedy the error of the California Supreme Court and of other state courts that may rely upon the decision below.

Nor should First Interstate's verdict cause this Court to be sanguine. First, of course, a national bank should be required neither to bow to state regulation in this area nor to pay the high price of obtaining a favorable verdict.

Second, there is no analytic distinction between this

service — processing an overdrawn check and considering whether to extend credit to the customer — and other bank services. The evidence in the First Interstate case was that the bank performs about 200 separate services. Other plaintiffs may sue First Interstate or other national banks in an attempt to learn about other bank costs and to limit other service fees.

Third, jury verdicts are unlikely to remain consistent from one national bank to the next. For instance, expert testimony in First Interstate's trial pegged the "cost" of an NSF check all the way from 92c to $7.33 during the relevant period, depending on what elements were included. Among the many vigorously disputed elements of costs, for example, was the loss resulting from customers' failure to repay overdrafts. In the event juries reach the cost-price relationship question, they can be expected to give widely varied answers as to each element of cost. Just in Oregon, the five pending cases could, and probably would, yield five different ways of determining "cost." The necessary result of the California decision will be *non-uniform regulation* of national banks.

Expert testimony in the First Interstate trial highlights the effects of attempting to regulate national bank pricing. Competition in the market for demand deposit accounts has increased dramatically since deregulation began in 1980. In Oregon, competition among banks, and between banks and other types of financial institutions, is now vigorous. An artificial (lower than market) price for NSF checks would place

First Interstate in a more difficult market position. Because a low price would encourage a disaportionate number of NSF checks, merchants would become unwilling to accept First Interstate checks. This in turn, would impair the bank's ability to attract and retain customers and, thus, to remain financially sound.

C. There Are Conflicting Opinions on the Preemption Issue Among the States.

The California Supreme Court found no preemption. The trial court in Oregon similarly rejected federal preemption arguments, although the issue now is pending on appeal.

In contrast, New York's highest court has suggested (albeit not squarely held) that federal regulation preempts state control of NSF charges. In *Jacobs* v. *Citibank, N.A.*, 61 N.Y.2d 869, 462 N.E.2d 1182, 474 N.Y.S.2d 464 (1984), the court decided that summary judgment on behalf of the bank was proper. There, as in the present case and the *Tolbert* case involving this *amicus*, the plaintiffs challenged the amount of the bank's NSF charge under state law theories. The court wrote:

> "... To grant the relief requested by plaintiffs would be to impose a limit on the amount Federally chartered banks can charge for processing overdrafts. This is a task more properly left to the Comptroller of the currency who has decided that '[a]ll charges to customers should be arrived at by each bank on a competitive basis'. (12 CFR 7.8000[a].)" 474 N.Y.S.2d at 465.

New York's approach, then, conflicts with the determination of the California Supreme Court below.

D. This Case Involves a Substantial, Undecided Federal Question.

The issue presented here is a substantial federal question under the Supremacy Clause. Its importance is demonstrated in the remainder of this brief and in the Jurisdictional Statement of Crocker National Bank. This Court has never answered the question, nor even a very closely analogous one.

Indeed, it has been many years since this Court considered a federal preemption issue regarding banks, *see Franklin Nat. Bank of Franklin Square* v. *People*, 347 U.S. 373 (1954), or discussed the history and philosophy of the National Banking Act. *see First Nat. Bank of Logan* v. *Walker Bank & T. Co.*, 385 U.S. 252 (1966). In the interim, with deregulation, the national banking laws have undergone significant change. Nor have market conditions for national banks remained static in the past 20 years. Comptroller's regulations have developed, and this Court's interpretation of preemption has evolved, *see Fidelity Federal Sav. & Loan Ass'n* v. *De La Cuesta*, 458 U.S. 141 (1982). In view of this changing legal, regulatory, and economic environment, guidance from this Court is essential for national banks.

II

THE SUPREMACY CLAUSE BARS STATE LIMITS ON NATIONAL BANK NSF CHARGES BECAUSE SUCH RESTRICTIONS STAND AS AN OBSTACLE TO THE ACCOMPLISHMENT OF THE FULL PURPOSES AND OBJECTIVES OF CONGRESS.

A. State Restriction of NSF Charges Stands as an Obstacle to the Accomplishment of the Full Purposes and Objectives of Congress.

Conflict preemption exists whenever state law presents an obstacle to the accomplishment of the full purposes and objectives of Congress. There is a comprehensive federal statutory scheme regarding banking. A state limit on NSF charges would present an obstacle to many of the federal objectives in this statutory scheme.

Several of the Congressional objectives that would be impeded are discussed in the Jurisdictional Statement of Crocker National Bank:

(1) The National Banking Act empowers national banks to receive deposits and grants them all necessary incidental powers. 12 U.S.C. § 24 (Seventh). State restrictions on actions related to the deposit-taking power are an obstacle to complete attainment of this goal.

(2) In 1980 [4] and 1982, [5] Congress phased out all limits on the rate of interest a federally insured bank could give and required them to pay market rates for deposits. In doing so, Congress expressly recognized that deregulation would require financial institutions to increase service charges on deposits, as well as interest rates on loans, in order to afford to pay market rates on deposits. State limits on NSF charges impede this policy.

(3) The National Banking Act and supporting regulations have established an intricate system to ensure the safety and soundness of national banks. One element Congress carefully balanced is service charges. If successful, the present suit and others like it would alter the balance and thus interfere with Congressional objectives.

(4) This lawsuit and similar ones interfere with the Comptroller's exclusive visitorial authority over national banks, because national bank records would be subject to inspection to see if NSF charges are "cost justified."

An additional Congressional objective impeded by this suit (and the similar ones filed elsewhere) is the general federal power to control national bank interest

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[4] Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, 94 Stat. 132; 12 U.S.C. § 3503.

[5] Garn-St. Germain Depository Institutions Act of 1982, Pub. L. No. 97-320, 96 Stat. 1469.

rates. For over 100 years, federal law has set interest rate ceilings for national banks. The ceiling set under federal law is usually the maximum rate allowed general lenders under the state law of the state where the national bank is located. *See* 12 U.S.C. § 85; *Hiatt* v. *San Francisco National Bank*, 361 F.2d 504 (9th Cir.), *cert. denied*, 385 U.S. 948 (1966); *Daggs* v. *Phoenix National Bank*, 177 U.S. 549 (1900).

Interest is the charge banks make for their principal service, lending money. Banks supplement their income from lending by providing associated services, such as checking accounts, for which other charges are made. If Congress alone may regulate the charge for lending money, it is implicit that states may not regulate national banks' similar charges. This is particularly true with respect to charges for processing NSF checks, because many authorities consider such checks to be unauthorized loan applications. *See Brady on Bank Checks* § 17.1 at p. 17-2 (5th ed. 1979) ("Overdrafts are said to be in the nature of loans not made in a creditable way . . ."); *Hoffman* v. *Security Pac. Nat. Bank*, 121 Cal. App. 3d 964, 176 Cal. Rptr. 14, 16 (1981) ("[S]tatutes governing the obligations of banks and their depositors, which are incorporated into and become part of the contract between a bank and its depositors . . ., treat an overdraft as an application for advance credit rather than as a breach of an express or implied covenant."). Thus, state regulation of NSF charges interferes with Congress's intent to regulate interest charged by national banks.

To summarize, the relief the plaintiff sought would require a state court to evaluate the workings of a national bank and make a determination as to the bank's costs and profitability. The plaintiff has asked a state court to pierce the very heart of a national bank and weigh the appropriateness of the means the bank uses to sustain itself. Such action impermissibly interferes with the federal structure that Congress established for the sanctity and soundness of national banks.

B. 12 C.F.R. § 7.8000 Directly Conflicts with State Limits on NSF Charges.

Even if the federal statutory scheme described above did not exist, the plaintiff's claim is preempted because of actual conflict between the recovery sought and 12 C.F.R. § 7.8000.[6] The Comptroller's ruling directs that a national bank set service charges using its business judgment. Under the rule, a national bank may consider profit motive and deterrence of frequent NSF check writing. The most recent statement of federal policy, set out in Crocker National Bank's Jurisdictional Statement and Appendix, comports with federal policy for over 20 years that national banks may consider noncost or market factors in setting service charges.

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[6] The *Comptroller's Handbook for National Bank Examiners* similarly recognizes that a national bank might levy a non-cost-based charge for NSF checks. *See, e.g., id.* at § 301.1 at 2 (1977) (overdraft charges should discourage frequent writing of NSF checks).

On March 5, 1962, then-Comptroller James J. Saxon issued an interpretive ruling regarding service charges — 12 C.F.R. § 7.2 (Appendix B). This ruling directed national banks to set their fees independently and not collusively. The regulation also specified *how* a national bank was to set its prices when conducting its independent review. It directed a bank to consider *both* "the individual bank's costs *and its competitive position.*" (Emphasis added.) In other words, the Comptroller expressly authorized national banks to consider market factors when setting their service charges.

Comptroller Saxon's 1962 ruling was reaffirmed in 1971 by Comptroller William B. Camp. At that time, the Comptroller performed a comprehensive reevaluation of various policies relating to national banks. Many policies were revised or deleted. Section 7.2, however, was readopted as § 7.8000 (Appendix C); the Comptroller reaffirmed in § 7.8000 the federal commitment to national bank service charges set on a "competitive" basis. New York's highest court recently recognized this feature of the 1971 ruling. In February 1984, the New York Court of Appeals relied on this 1971 ruling in rejecting plaintiffs' NSF challenge. *See Jacobs* v. *Citibank*, N.A., 61 N.Y.2d 869, 474 N.Y.S.2d 464, 462 N.E.2d 1182 (1984) (The task of deciding what NSF charges are appropriate is "more properly left to the Comptroller of the currency who has decided that '[a]ll charges to customers should be arrived at by each bank on a competitive basis'." 474 N.Y.S.2d at 465 (quoting 12 C.F.R. § 7.8000).).

Contemporaneous sources confirm two important points. First, the Comptroller wanted market factors, not just cost, to govern national bank service charges. Second, the Comptroller consciously included NSF charges among the matters within the purview of federal regulation. *See* text of November 5, 1963 letter of Comptroller Saxon (Appendix A).

In short, this plaintiff's lawsuit and others like it conflict with the long-standing federal policy to use a noncost, market approach to national bank service charges, including NSF charges. This long-standing policy provides an independent basis for preemption.

III

THE CALIFORNIA DECISION VIOLATES THE SUPREMACY CLAUSE BECAUSE CONGRESS HAS OCCUPIED THE RELEVANT FIELD.

The resolution of field preemption cases often turns on how the field is defined. *See Silkwood* v. *Kerr-McGee Corp.*, 464 U.S. 238 (1984) (majority found no preemption because Congress did not intend to disturb state remedies; dissent defined the field differently and argued that there was preemption because Con-

gress did not specifically exempt punitive damages from preemption). A "field" need not be very broad. *See City of Burbank* v. *Lockheed Air Terminal, Inc.*, 411 U.S. 624 (1973) (regulation of noise from aircraft was relevant field). In this case, Crocker National Bank should prevail regardless of how the field is defined.

If the "field" is defined narrowly, this Court must ask, "Has federal law occupied the field of the appropriate amount for NSF charges?" Because the answer to this question is an unequivocal "yes," *see* 12 C.F.R. § 7.8000, field preemption exists.

Using a broader definition, the Court should ask, "Has federal law occupied the field of the incidental acts necessary to a national bank's power to receive deposits?" The answer to this question, too, is an unequivocal "yes" under the holding of *Franklin Nat. Bank of Franklin Square* v. *People*, 347 U.S. 373, 378 (1954) (national bank could advertise as a "savings" bank in contravention of New York state law; no indication that Congress intended this phase of national banking to be subject to local restrictions). *See also Easton* v. *Iowa*, 188 U.S. 220, 229 (1903) (national banks exempt from state conditions on receipt of deposits); *First Nat. Bank of San Jose* v. *State of California*, 262 U.S. 366, 369 (1923) (state escheat law preempted by deposit-taking function of national banks). Thus, field preemption exists regardless of how the field is described.

CONCLUSION

This *amicus*, like other national banks, now faces a fundamental conflict between federal and state law. Federal laws, regulations, and policies mandate market pricing, while state courts, including the courts below, are attempting to alter and limit the market pricing mechanism for bank services.

For the reasons stated above, *amicus curiae* First Interstate Bank of Oregon, N.A., urges this Court to consider the merits of this case and either (1) set the matter for oral argument or (2) reverse the California Supreme Court decision summarily.

Respectfully submitted,

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January 14, 1986

APPENDIX A

Gwin-Examiner
November 5, 1963

Dear Mr. Chairman:

This Office takes the position in regard to bank service charges that this is a matter to be governed by banking judgment as controlled by competitive factors in the arena in which the banks operate. If a particular bank imposes service charges that are too high, a rival bank would be able to take away a great deal of its business by offering a lower rate. Inasmuch as our society is grounded on the principle of free competition, strong competitors rather than government regulation in the local banking picture are the surest safeguards against arbitrary and unreasonable charges by an individual institution. Only when the competitive arena is a closed market and dominated by one or a few organizations does government regulation become the only answer to improper service charges and the like by banks.

The same argument would also apply to unreasonable penalties for checks drawn without sufficient funds even though this might be a more rarely used and less well-known policy of the bank. If depositors are treated unfairly in this matter at an institution, as this becomes known, more and more of the banking public will begin to deal with competitors.

This Office, therefore, does not attempt to regulate the charges that National Banks impose on their cus-

tomers. If, of course, in this area a case of gross abuse of discretion akin to fraud or the like were to be brought to the attention of our examiners, this Office would take appropriate regulatory action. In regard to Mr. Kimmel's letter, it would be difficult to make any particular comment without knowing and having proof of all the facts.

Sincerely,

/S/ JAMES J. SAXON

JAMES J. SAXON
Comptroller of the Currency

HONORABLE DENTE B. FASCELL
Chairman, Legal and Monetary Affairs Subcommittee of the
Committee on Government Operations
House of Representatives
Washington, D.C.

Enclosure

TGraham: 1m 11/4/63

APPENDIX B

Title 12 — BANKS AND BANKING

Chapter 1 — Bureau of the Comptroller of the Currency, Department of the Treasury

PART 7 — INTERPRETATIONS

National Banks; Service Charges

Part 7, Chapter I, Title 12, of the Code of Federal Regulations of the United States of America is hereby amended by adding a new § 7.2 as follows:

§ 7.2 *National banks; service charges.*

The Comptroller of the Currency has issued formal instructions concerning the service charges of banks as indicated in the following letter addressed to the presidents of all national banks:

To the presidents of all national banks:

So that there may be no misunderstanding with respect to the policy of this Office concerning the service charges of banks, I am issuing these formal instructions to all national banks.

Agreements, arrangements, undertakings, understandings, etc., among banks, through clearing houses or otherwise, concerning service charges are not permissible in any form. It is the responsibility of the

Board of Directors of each national bank to terminate promptly any of these practices which it may now be following.

Wherever a national bank has been involved in any of the practices cited, it should now review its scale of service charges independently of any other bank, and take appropriate corporate action to re-establish a scale of service charges independent of any relationships with any other bank. In taking this action, it is appropriate to make such changes in the scale of service charges as are deemed necessary or desirable in the light of the individual bank's costs and competitive position. This review and re-establishment of the scale of service charges should be undertaken, even though there may have been no overt or implicit agreement, wherever there have been discussions of such charges among banks or their officers, either independently or in group meetings, or where the scale of service charges was adopted with knowledge of prospective adoption of similar charges by competitor banks.

It is recognized that identical charges for identical services may occur where there are no agreements or understandings among banks. Nevertheless, wherever this occurs, each national bank must be prepared to demonstrate conclusively that its scale of service charges was decided unilaterally, and not on the basis of any agreement or understanding, or even of discussion, among banks or their officers.

Our examiners have been instructed to explore,

regularly and in detail, the methods by which the existing scale of service charges was determined by each national bank. At the time of the next examination of your bank, inquiry shall be made to determine whether appropriate action has been taken, where necessary, to conform to these instructions.

(R.S. 5240; 12 U.S.C. 1, 481)

Dated: March 5, 1962.

[SEAL]

JAMES J. SAXON
Comptroller of the Currency

[F.R. Doc. 62-2336; Filed, Mar. 8, 1962; 8:49 a.m.]

APPENDIX C

§ 7.8000 *Charges by banks.*

All charges to customers should be arrived at by each bank on a competitive basis and not on the basis of any agreement, arrangement, undertaking, understanding or even discussion among banks or their officers.

Dated: August 20, 1971

[SEAL]

WILLIAM B. CAMP
Comptroller of the Currency

[F.R. Doc. 71-12412; Filed, 8-25-71; 8:45 a.m.]